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Washington, D.C. 20520

12 JUN 1975


Mr. John F. Blake
Deputy Director for Administration
Central Intelligence Agency
Room 7D26 - Headquarters Bldg.
Washington, D. C. 20505

Dear Mr. Blake:

You will find enclosed two papers just received from Warren Brecht on the question of taxation of overseas allowances. I would appreciate your giving me any comments you wish to make on the papers either by phone or in writing before or at the meeting of the Inter-Agency Committee on Overseas Allowances scheduled for Monday, June 16 at 2:15 p.m. in room 6320, Department of State. You will note that Dave Foster feels that Committee hearings may begin this month.

John Thomas would also like you to consider whether this question is a proper one for the Interagency Committee on Overseas Allowances or whether it should be handled in another forum, perhaps the Office of Management and Budget.

Sincerely,


James Stromayer
Director
Allowances Staff

Encl:

UNITED STATES GOVERNMENT

Department of the Treasury
Washington, D.C.

Memorandum

TO : Warren F. Brecht
Assistant Secretary (Administration)

DATE: June 2, 1975

FROM : David S. Foster *DSF*
Deputy International Tax Counsel

SUBJECT: Overseas Allowances and Benefits--Possible Alternative
Tax Treatment

Under present law, section 912 of the Internal Revenue Code provides tax exemption for overseas allowances paid to Federal employees with respect to travel, education, housing, and cost of living. For the private sector, section 911 of the Code provides tax exemption for up to \$25,000 of income earned abroad by foreign residents.

Last year, the Ways and Means Committee reported out a bill which would have repealed sections 912 and 911 over a three-year period beginning in 1975. The bill would have replaced these exemptions with a new deduction for tuition payments for dependents of foreign residents, limited to \$100 per month per dependent, and with a new exemption for "municipal-type" services provided by an employer to his employees (e.g., schools and roads in company towns).

When the Ways and Means Committee takes this matter up again in the next few months, it might be helpful if Treasury could suggest alternatives to sections 912 and 911, i.e., alternative provisions to take account of the increased expenses related to foreign assignments. Specifically, we might consider the following program:

(1) Education. The deduction for tuition adopted last year by the Committee would be broadened by removing the dollar limit and by adding a deduction for transportation to and from school. (The deduction would still not include room and board.)

(2) Travel. Government employees would be allowed an exclusion or deduction for travel expenses incurred in connection with home leave. This deduction would not apply to the private sector. (Other travel expenses should be excludible under general principles.)



Last fall Treasury did not really take much of a position either way; i.e., they did not oppose the repeal of Sections 911 and 912. They did, however, in conjunction with the Joint Committee on Internal Revenue Taxation, believe that a further examination should be made of certain deductions. In the end, the only two deductions affected were educational allowances (limited to certain amounts) and certain municipal type services (primarily directed toward company-run towns and therefore having little or no impact on the government employees).

Looking Ahead

I asked whether there would be formal hearings, an opportunity to hear arguments, written positions, etc. Patrick and Foster indicated that any or all of these were possible, although they were not sure at this point what the process would be.

I expressed my concern that they be mindful of my role as a member of the interagency task force looking for equitable but fair treatment of Treasury employees overseas vis-a-vis overseas employees of other agencies. At the same time, I did not want to unduly influence our tax policy people on tax policy matters having to do with overseas people. They appreciated my role and did not see what they were doing as being inconsistent with the interagency task force; i.e., while different groups and individuals perhaps have different motives for wanting certain things in or out, from a tax policy standpoint they agreed that it was appropriate for Treasury to take a hard look at the equities as well as the inequities of existing overseas benefits and their tax effect, with the end objective of coming up with a package that makes sense.

Since the interagency task force is actively working but is undoubtedly some months away from completing their findings and recommendations, I asked what the likelihood would be of getting the Ways and Means Committee to defer consideration of Sections 911 and 912 until later in the session. Both Patrick and Foster did not think this was realistic since, from their experience, the Committee is inclined to take things up in the order it prefers.

They suggested that a better approach perhaps would be to try to influence the effective dates when certain changes in benefits would begin to occur. For example, a 3-year phase out beginning in 1977. By delaying the effective dates, either or both of the following might well occur:

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1. The Congress at a later date might be willing to extend the expiration dates for certain phase-outs as a rider to another tax bill, if by then we have a compelling case for what should be substituted.
2. The mere delay in effective date itself would allow time in a subsequent fiscal year to seek additional appropriations or put in whatever remedies might be needed to offset the loss of a tax benefit where the task force and the Congress felt that some kind of benefit should be provided.

Finally, Patrick and Foster indicated that even if the House were to pass a tax bill by December, it is unlikely that the Senate would do the same this year. Therefore, there still would be an opportunity to get the recommendations of the interagency task force to the Congress before a final tax reform act was passed, probably in 1976.

Ideally, we all agreed that the interagency task force study and recommendations should be completed and available to the Ways and Means Committee before action is taken on Section 912. Recognizing the facts of life, however, we also agreed that it would be better if Treasury could at least make some positive suggestions to the Committee, even if it had to be prior to the completion of the full study. This would seem preferable to taking a passive position and not reacting one way or the other.

With this in mind, Dave Foster agreed to prepare a quick paper on some of the existing allowances and what Treasury's tax policy people might be willing to support. It is my impression that we are still at the "idea" stage and these suggestions are really more for discussion purposes than official Treasury tax policy at this point.

We agreed that my notes, together with Dave Foster's suggested ideas for refining the overseas allowances, would be sent to John Thomas for his review and further discussion.



ASSISTANT SECRETARY

May 28, 1975

MEMORANDUM TO THE FILE

From: Warren F. Brecht *WFB*
Assistant Secretary (Administration)

Subject: Meeting with Robert J. Patrick, Jr. (International Tax Counsel) and David S. Foster (Deputy International Tax Counsel) on the status of Sections 911 and 912 of the IRS Code and the impact on the interagency study of overseas allowances and benefits.

Today I met with Bob Patrick and Dave Foster to find out what the likelihood was of Sections 911 and 912 being repealed, modified or whatever as part of general tax reform legislation during this session of the Congress. This meeting was in response to John Thomas' call the previous week in which he said he understood that the general subject of repealing certain overseas tax benefits was likely to be addressed by the House Ways and Means Committee shortly.

Foster indicated that whereas the previous week it appeared that the Ways and Means Committee would begin hearings early in June, it now appears that the earliest would be the end of June since Congress never did pass the energy bill yet.

Background

To refresh my memory, Patrick and Foster mentioned that last fall the House voted an outright repeal of 911 (the private sector employees overseas) and also 912 (government employees overseas). Basically, this eliminated certain tax benefits which the two groups have received up until now.

It is difficult to know just what the Ways and Means Committee will recommend this time, since it is a substantially different Congress and the Ways and Means Committee alone has a dozen new members. Therefore, whether the new Congress will follow the tentative actions of the old Congress by repealing either or both 911 and 912 remains problematical. Patrick and Foster believe, however, that 911 will probably still be repealed. While 912 admittedly did not get the same degree of attention or study last time, there still was a general feeling to treat the government employees in the same manner. If this is done, 912 would likely be repealed also.

(3) Housing. Reimbursements for housing costs would be taxable. However, with respect to government employees, the taxable amount would not be permitted to exceed the rental value of typical housing in the Washington, D.C. area. This limit would be imposed because in some areas of the world reasonable U.S.-type housing is extremely expensive and because often U.S. employees stationed abroad are required to have large houses suitable for extensive entertainment. One reasonable way of arriving at the rental value of typical housing in the Washington, D.C. area would be to assume that it is equal to 25 percent of salary. (This provision would not apply to the private sector.)

(4) Cost-of-living. No additional cost-of-living exclusion or deduction would be provided. The housing provision outlined above would represent a significant cost-of-living adjustment. Also, Federal employees typically have commissary privileges, and it is difficult to give a cost-of-living adjustment to Federal employees without giving it to private employees.

(5) Standard Deduction. The Internal Revenue Code would be amended so that a standard deduction could be taken at the same time as a foreign tax credit. This would give significant relief to low and middle income (\$7,000-\$20,000) employees. This would apply to both public and private employees.

(6) Delay. The repeal of sections 911 and 912 would be delayed by two years from 1975 to 1977. One of these two years is appropriate because of the delay in the legislation and the other year is appropriate to give a chance for adjustments to be made in the structure of Federal overseas allowance and benefits. Sections 912 and 911 would be phased out, so that two-thirds of the exclusions would be available in 1977 and one-third would be available in 1978.

We may wish to discuss the above ideas with John Thomas at State.

cc: Mr. Hickman
Mr. Patrick